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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:02

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Date:

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LEGEND

Distributing =

State A =

Date B =

Date C =

Business D =

Family =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

Shareholder 4 =

Shareholder 5 =

Grantor Trust =

Controlled 1 =

Controlled 2 =

Controlled 3 =

Controlled 4 =

Trust 1 =

Trust 2 =

Trust 3 =

Trust 4 =

a =

b =

c =

d =

e =

f =

X =

Y =

Dear :

This letter responds to your December 1, 2007, letter requesting rulings as to the federal income tax consequences of a series of proposed transactions. The information provided in that request and in later correspondence is summarized below.

The rulings contained in this letter are based upon facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether any distribution described below: (i) satisfies the business purpose requirement of section 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of a distributing or controlled corporation or both (see section 355(a)(1)(B) of the Internal Revenue Code and Treas. Reg. section 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in a distributing or controlled corporation (see section 355(e) and Treas. Reg. section 1.355-7).

SUMMARY OF FACTS

Distributing is a State A corporation that was organized as a subchapter C corporation on Date B. On Date C (less than 10 years ago), Distributing elected to be taxed as a subchapter S corporation for federal income tax purposes. Distributing has two classes of common stock (Series A and B) that are identical in all respects, except that each share of Series A stock is entitled to X votes and each share of Series B stock is entitled to Y votes. All of the Distributing stock is owned by members of Family. Shareholder 5 is the parent of each of Shareholders 1 through 4. The Series A stock of Distributing is owned a% by Shareholder 1, a% by Shareholder 2, a% by Shareholder 3, b% by Shareholder 4, and c% by Shareholder 5. The Series B stock of Distributing is owned d% by each of Shareholders 1 through 4. Distributing has no securities outstanding.

Shareholder 5, the majority shareholder of Distributing, holds all of her Distributing stock in a revocable trust ("Grantor Trust"). Shareholder 5 is the grantor of Grantor Trust and is treated as the owner of Grantor Trust under sections 674 and 676. Shareholder 5 is the sole surviving trustee of Grantor Trust. Grantor Trust will terminate upon Shareholder 5's death. Upon the death of Shareholder 5, the trustee will distribute the assets in Grantor Trust to anyone, including Shareholder 5's estate, either outright or in trust, as Shareholder 5 appoints. In default of the exercise of Shareholder 5's power of appointment, the assets in Grantor Trust will be distributed equally among Shareholders 1 through 4.

Distributing is directly engaged in Business D. Distributing has submitted financial information which indicates that Business D has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

PROPOSED TRANSACTIONS

For what are represented to be valid business reasons, Distributing has proposed the following transactions (the “Proposed Transactions”):

- (i) Distributing will create Controlled 1, Controlled 2, Controlled 3, and Controlled 4 (collectively, the “Controlled corporations”).
- (ii) Distributing will transfer all of its assets to the Controlled corporations in exchange for all of the stock of each of the Controlled corporations and the assumption by each of the Controlled corporations of the liabilities associated with the assets transferred (collectively, the “Contributions”).
- (iii) Distributing will distribute pro rata all of its stock in each of the Controlled corporations to Shareholders 1 through 5 in exchange for all of the stock of Distributing held by Shareholders 1 through 5 (collectively, the “Distributions”). Each of the Controlled corporations will elect to be taxed as a subchapter S corporation on the first available date after the Distributions.
- (iv) Distributing will liquidate.

Shareholder 5 will establish four irrevocable grantor trusts; Trust 1, Trust 2, Trust 3, and Trust 4 (collectively, the “Trusts”). Distributing represents that Shareholder 5 will be the grantor of each of the Trusts and will be treated as the owner of each Trust’s assets under section 671. Shareholder 1 will be the sole beneficiary of Trust 1, Shareholder 2 will be the sole beneficiary of Trust 2, Shareholder 3 will be the sole beneficiary of Trust 3, and Shareholder 4 will be the sole beneficiary of Trust 4.

Shareholder 5 will cause Grantor Trust to transfer e% of its stock in Controlled 1 to Trust 1, e% of its stock in Controlled 2 to Trust 2, e% of its stock in Controlled 3 to Trust 3, and e% of its stock in Controlled 4 to Trust 4 (the “Gift Transactions”). Shareholder 5 will cause Grantor Trust to sell f% of its stock in Controlled 1 to Trust 1, f% of its stock in Controlled 2 to Trust 2, f% of its stock in Controlled 3 to Trust 3, and f% of its stock in Controlled 4 to Trust 4 in exchange for promissory notes from each Trust (the “Sale Transactions”). Distributing has represented that the Gift Transactions and the Sale Transactions are disregarded for federal income tax purposes.

Shareholder 5's estate plan provides that her ownership interests in each of the Controlled corporations will be separated, so that Shareholder 1 will only inherit the stock of Controlled 1, Shareholder 2 will only inherit the stock of Controlled 2, Shareholder 3 will only inherit the stock of Controlled 3, and Shareholder 4 will only inherit the stock of Controlled 4.

REPRESENTATIONS

The taxpayer makes the following representations regarding the Proposed Transactions:

- (a) Neither Business D nor control of any entity conducting this business was acquired during the five-year period ending on the date of the Distributions in a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part.
- (b) The fair market value of the stock of each of the Controlled corporations to be received by each shareholder of Distributing will be approximately equal to the fair market value of the Distributing stock surrendered by each shareholder in exchange therefor.
- (c) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (d) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (e) Following the Proposed Transactions, the Controlled corporations will each continue, independently and with its separate employees, the active conduct of its share of all the integrated activities of Business D conducted by Distributing prior to consummation of the Proposed Transactions.
- (f) The distribution of the stock of each of the Controlled corporations is carried out for the following corporate business purposes: (i) to implement business succession planning; and (ii) to avoid shareholder deadlock after implementation of the plan by allowing each shareholder in the post-transition structure to independently manage his or her portion of Distributing's business.

- (g) The Proposed Transactions are not used principally as a device for the distribution of the earnings and profits of Distributing or the Controlled corporations.
- (h) For purposes of section 355(d), immediately after the Distributions, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the date of the Distributions.
- (i) For purposes of section 355(d), immediately after the Distributions, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of any Controlled stock entitled to vote or 50 percent or more of the total value of the shares of all classes of any Controlled stock, that was either (i) acquired by purchase (as defined in section 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the date of the Distributions.
- (j) Any liabilities assumed (within the meaning of section 357(d)) by the Controlled corporations in the Proposed Transactions were incurred in the ordinary course of business and are associated with the assets being transferred.
- (k) With respect to each Contribution to a Controlled corporation, the total adjusted bases and the total fair market value of the assets transferred to the Controlled corporation by Distributing in the Proposed Transactions will exceed the sum of the amount of any liabilities assumed (within the meaning of section 357(d)) by the Controlled corporation in the exchange.
- (l) No intercorporate debt will exist between Distributing and any of the Controlled corporations at the time of, or subsequent to, the Distributions.
- (m) Payments made in connection with all continuing transactions, if any, between any of the Controlled corporations will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (n) No parties to the Proposed Transactions are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).

- (o) The Distributions are not part of a plan or series of related transactions (within the meaning of Treas. Reg. section 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest (within the meaning of section 355(d)(4)) in either Distributing or any of the Controlled corporations (including any predecessor or successor of Distributing or any of the Controlled corporations).
- (p) Immediately after the Distributions, either (i) no person will hold a 50-percent or greater interest (within the meaning of section 355(g)) in the stock of Distributing or any of the Controlled corporations who did not hold such an interest immediately before the distribution, or (ii) neither Distributing nor any of the Controlled corporations will be a disqualified investment corporation (within the meaning of section 355(g)(2)).

RULINGS

Based solely on the information submitted and the representations set forth above, we rule as follows:

- (1) Each Contribution, together with its respective Distribution, will be a reorganization within the meaning of section 368(a)(1)(D). With respect to each such reorganization, Distributing and the respective Controlled corporation will be “a party to a reorganization” within the meaning of section 368(b).
- (2) No gain or loss will be recognized by Distributing on the Contributions (sections 357(a) and 361(a)).
- (3) No gain or loss will be recognized by any of the Controlled corporations on the Contributions (section 1032(a)).
- (4) The basis of each asset received by each of the Controlled corporations in the Contributions will equal the basis of that asset in the hands of Distributing immediately before the Contributions (section 362(b)).
- (5) The holding period of each asset received by each of the Controlled corporations in the Contributions will include the period during which Distributing held the asset (section 1223(2)).

- (6) No gain or loss will be recognized by (and no amount will be included in the income of) Shareholder 1, Shareholder 2, Shareholder 3, Shareholder 4, or Shareholder 5 on their receipt solely of the stock of the Controlled corporations in the Distributions (section 355(a)).
- (7) No gain or loss will be recognized by Distributing in connection with the Distributions (section 361(c)(1)).
- (8) With respect to each of Shareholders 1 through 5, the aggregate basis of the stock of the Controlled corporations in their hands after the Distributions will equal the aggregate basis of the Distributing stock surrendered in exchange therefor, and this aggregate basis will be allocated between the stock of the Controlled corporations in proportion to the fair market value of each immediately following the Distributions in accordance with Treas. Reg. section 1.358-2(a) (section 358(a) and (b)(2)).
- (9) The holding period of the stock in each of the Controlled corporations received by each of Shareholders 1 through 5 in the Distributions will include the holding period of the Distributing stock surrendered in exchange therefor, provided the Distributing stock was held as a capital asset on the date of the Distributions (section 1223(1)).
- (10) The earnings and profits of Distributing (if any) will be allocated to each of the Controlled corporations in accordance with section 312(h) and Treas. Reg. section 1.312-10(a).
- (11) Each of the Controlled corporations will be subject to section 1374 with respect to any asset transferred from Distributing to the Controlled corporations to the same extent Distributing was subject to section 1374 with respect to such asset. For purposes of section 1374, the recognition period of each of the Controlled corporations will be reduced by the portion of Distributing's recognition period that expires prior to Distributing's transfer of the assets (section 1374(d)(8) and Ann. 86-128, 1986-51 I.R.B. 22).

CAVEATS

No opinion is expressed about the tax treatment of the Proposed Transactions under other provisions of the Code and regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Proposed Transactions that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding:

- (i) Whether the Distributions satisfy the business purpose requirement of Treas. Reg. section 1.355-2(b);
- (ii) Whether the Distributions are used principally as a device for the distribution of the earnings and profits of Distributing or the Controlled corporations;
- (iii) Whether the Proposed Transactions are part of a plan (or series of related transactions) under section 355(e)(2)(A)(ii);
- (iv) Whether Distributing's election to be taxed as a subchapter S corporation is valid; whether the Controlled corporations are otherwise eligible to be taxed as subchapter S corporations; and whether the Controlled corporations' elections to be taxed as subchapter S corporations will be valid under section 1362(a);
- (v) The gift and estate tax treatment of the proposed transactions, including whether the Gift Transactions and the Sale Transactions constitute separate transactions for gift tax purposes and the extent to which the Gift Transactions and the Sale Transactions constitute transfers for adequate consideration in money or money's worth;
- (vi) Whether the Trusts are trusts described in subpart E of part I of subchapter J.

PROCEDURAL STATEMENTS

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this letter ruling.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Frances L. Kelly
Assistant to the Branch Chief, Branch 2
(Corporate)